STATEMENT OF
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BEFORE
House Government Reform Committee

HEARING ON
Final Revisions to OMB Circular A-76

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Mr. Chairman and members of the Committee, my name is Don Dilks and I am President of DDD Company. My company provides a wide variety of logistical services to its Government and industry clients, specializing in mail processing and distribution warehousing, order fulfillment and messenger services.

I also serve as Chairman of the Executive Committee for the Contract Services Association of America (CSA), which is the premier industry representative for private sector companies that provide a wide array of services to Federal, state and local governments. Our members are involved in everything from maintenance contracts at military bases and within civilian agencies to high technology services, such as scientific research and engineering studies. Many of our members are small businesses, including 8(a) certified companies, small disadvantaged businesses, women-owned, HUBZONE, and Native American owned firms. The goal of CSA is to put the private sector to work for the public good.

General Overview

Thank you for the opportunity to be here today and to share an industry perspective on the Revisions to Circular A-76 which were released last month by the Office of Management and Budget (OMB). The Revisions represent an improvement in the competitive sourcing process and should increase private sector competition for Government services, which is good for the taxpayer. I am hopeful that these Revisions put us back on course and will encourage companies to jump back into the competition – that will be the ultimate measure of success for the revised A-76 process. Competition is a key tenet of the President's Management Agenda, which is aimed at improving the performance of Government and making Government more citizen-centered, results-oriented and market-based.

CSA has worked with and on (including previous re-writes of) Circular A-76 since the Association's founding in 1965 – at a time when no one else was interested in even talking about the Circular or making it work. Now, public-private competitions are a much discussed issue, and key to agency performance. Our years of persistence are paying off. Certainly, the recent increased attention has not been without its challenges, but we will continue to tell our story of the benefits to be achieved from this process.

As we have consistently noted (in testimony and congressional letters), CSA is interested in fairness and best value. More and more of our companies have walked away from competitions with the Government because of chronic problems found in the implementation of the "old" system. As I already stated, I am hopeful that these Revisions put us back on course and will encourage companies to jump back into the competitions.

The intent behind A-76 (*i.e.,* to establish a process for public-private competitions) has never really been in question. But, implementation of the "old" A-76 Circular turned it into a lengthy, expensive and unnecessarily convoluted process, leading all sides to declare that it was unfair. Many companies would no longer bid on A-76 competitions under the old rules. Without active bidding by industry there is no true competition and the Government would then never know if it had gotten the best deal.

The Revisions are aimed at addressing this problem by tightening the timelines for competitions. They make the process fairer by treating the public sector proposals ("tender offers") like private sector bids and by evaluating all proposals, both public and private, under the same set of rules. Optimistically, these Revisions should lead to increased competition, producing not only cost savings for the Government but also encouraging innovation, which is the key to improving the quality of service delivery.

While the new rules are easier to navigate, and there appears to be greater clarity and consistency as well as enhanced accountability, implementation remains key – or, as we have seen happen too often in the past, good intentions will go down the drain. Fairly implementing this for public-private competitions will be a challenge, filled with nuances and potential pitfalls, but we stand ready to aggressively work with the Congress and the Administration to ensure the goals of the A-76 Revisions are fully achieved. This is the right thing to do.

Commercial Activities Panel

Much of the Circular A-76 Revisions are based on recommendations made by the Blue Ribbon Commercial Activities Panel (CAP), of which CSA member Mark Filteau of Johnson Controls, and public sector union leaders were members.

In its April 2002 report to Congress, the Panel unanimously adopted ten key principles that should guide agency sourcing policies. To varying degrees, these principles are reflected in the Revisions, particularly the following:

- Recognize that inherently governmental and certain other functions should be performed by Federal workers;
- Be based on a clear, transparent, and consistently applied process;
- Ensure that, when competitions are held, they are conducted as fairly, effectively, and efficiently as possible;

- Ensure that competitions involve a process that considers both quality and cost factors; and
- Provide for accountability in connection with all sourcing decisions.

These sourcing principles were used by the Panel to assess the A-76 process (as last revised in 1996) and make its recommendations, the most obvious one being the adoption of a process governed by the Federal Acquisition Regulations (FAR):

> *"That in order to promote a more level playing field on which to conduct public-private competitions, the government needs to shift, as rapidly as possible, to a FAR-type process under which all parties compete under the same set of rules."*

Shifting competitive sourcing to an approach governed by the FAR, the A-76 Revisions move to a process that is fair and time-tested with clear rules. Unlike the current A-76 rules, the FAR offers a well-documented process that has the confidence of both the Government and industry. Indeed, a system based on the FAR is one that Government procurement officials are most familiar.

Old versus New A-76 Process

In its April 2002 report to Congress, the CAP highlighted a common complaint against the "old" A-76 process:

> *"Both Federal employees and privates complain that the A-76 process does not meet the principles' standard of a clear, transparent, and consistently applied process."*

As implied in the CAP findings, private sector executives increasingly have concluded that the old A-76 process was so flawed, intrinsically unfair and biased toward the Government that it was not prudent business to devote marketing resources to public-private competitions. While A-76 procurements represent an important potential source of new business, companies must be persuaded that the competition will be reasonably fair before they will aggressively pursue A-76 opportunities; and they will only do so on a highly selective basis. However, in the past few years, participation by qualified companies has declined since the competitions were perceived as being biased toward the Government. That is unfortunate because it deprives the Government of valuable competition and because many of those companies have excellent business practices that could contribute significantly to improved infrastructure efficiency. Unfortunately, the real loser here is the taxpayer, because the perceived A-76 "gamesmanship" (in the old process) results in limited competition and ultimately potentially higher costs to the Government.

CSA members have consistently cited five areas in the old A-76 process that needed to be addressed and improved:

- **Fairness:** Companies need to know the competition will be fair from the outset. If the rules are different for in-house bids, and companies are greeted by bias and hostility from the leadership overseeing the competition, most companies will decline the opportunity. As the saying goes, "If you want competition, then you invite and attract competition."
- **Timing:** As commercial activity studies stretched out and procurements delayed, uncertainty plays havoc with individual contractor's ability to schedule bid and proposal resources. Delayed competitions are costly. Setting a schedule and meeting schedule milestones are important.
- **Cost Comparison:** Nothing is more important than a fair cost comparison and fair cost comparison procedures. If either is seen as unfair and the Government is continually accused of "gaming" the system, then contractors will not bid on future procurements. Nothing is more important than the integrity of the procurement process; unfortunately, a number of GAO A-76 protests have focused on whether fair cost comparisons were conducted.
- **Unlimited Attempts for the MEO:** Under the old process the in-house team was provided unlimited attempts to correct a flawed proposal and make it technically acceptable. This was not only unfair but added process delay. Most importantly, it allowed the MEO to "game" the system. By "low-balling" or submitting technically unacceptable proposals, the evaluating team (either the IRO or SSA) could continue to send back to the MEO its proposal to fix whatever is unacceptable. This fixing or "pulling up" process would continue until the in-house team submitted the very least technically acceptable proposal. When such a proposal is priced, by definition it should result in the lowest priced proposal possible, in a cost comparison. Even if a contractor submitted a proposal that also just met the bare minimum threshold of technically acceptability, it would be unlikely that the contractor could overcome the 10% conversion factor, which advantages the MEO. The result was a process under which the contractor loses every time.
- **Accountability:** A winning MEO must be held to performance standards and costs as proposed. Anything short of full accountability for the winning entity deprives the Government of getting the best proposal and destroys the integrity of the process.

CSA has never advocated that all Government services be contracted to the private sector. But as we continue to reinvent Government we must focus on competition. And that focus requires a balanced, responsible and unyielding commitment to exploring new ideas, challenging old prejudices and looking carefully at what services the Government must provide. It also requires a careful examination of who, inside or outside of Government, is best positioned to provide each service in the most efficient and effective way. This means, too, that the Government should adopt from the best of private enterprise those tools that foster the necessary incentives and rewards for high performance. And it must follow a fair process designed to protect the interests of the taxpayer and address the legitimate concerns of the current Government workforce while, at the same time, ensuring that the Government operates in a maximally efficient manner.

It is too early to tell whether CSA members and other private sector firms will jump back into the A-76 process. It is important to recognize that shifting to a FAR-type

process is not a cure for all the problems facing competitive sourcing. Significant issues remain. Cost comparisons between public and private sector bids will continue to demand careful scrutiny and fairness. Improvement is also needed in developing quality statements of work, the heart of the solicitation. Also, all competitors need to be ensured of equal access to relevant information, including workload data, in order to make credible proposals.

And there needs to be continued high-level agency support, along with an on-going dialogue between the agency and OMB. To a certain extent, this is recognized in the Revisions, which requires that agencies post lessons learned and best practices on SHARE A-76! Furthermore, Federal agencies should consider developing teams to provide consistent advice and training on preparing proposals for in-house competitions.

Comments on Final Circular A-76 Revisions

I believe the Revisions will improve the process in the following areas:

Fair Act Inventories

The Revisions spell out how agencies should develop their annual inventories as required by the Federal Activities Inventory Reform (FAIR) Act. And it requires agencies to inventory not only their commercial activities, but to include inherently governmental activities as well. This is important since it sheds additional sunshine on the Government's activities. Indeed, nothing in the FAIR Act ever prohibited the inclusion of inherently governmental activities on the inventory.

The one area that CSA continually found fault was the establishment of Reason Codes in the agencies' FAIR Act inventories. Challenges could be made to the inclusion or exclusion of a commercial activity but not to the application of a specific Reason Code. Our concern was that an agency could identify functions as commercial and, using the Reason Codes, protect the functions from competition. The Revisions now properly allow challenges to the applicability of Reason Codes. This will enhance agency accountability.

Time Frame

One area in particular that CSA has long promoted is shortening the time for the competitions – the revised Circular requires standard competitions to be completed within 12 months. This is definitely more reflective of a FAR-based process. In addition, predictable timeframes will facilitate the involvement of small businesses in the A-76 competition process because small businesses (with their limited credit line and marketing budgets) could rarely afford to participate in the previous A-76 process, which dragged out 2-4 years.

For the Government, the business case for outsourcing through the A-76 process has been made. Accordingly, it is in the Government's best interest to rapidly execute a

competition in order to quickly reduce costs and improve efficiencies. Lengthy competitions run counter to good business practices and end up costing American taxpayers unnecessary budget dollars.

In addition, the Revisions emphasize the preliminary planning that an agency must do "upfront" – this focuses on developing an acquisition strategy, prior to announcement for either a streamlined or standard competition. This, in turn, should assist agencies in developing better performance work statements and solicitations, etc.

Evaluation Factors

The process will be fairer by treating the public sector proposals like private sector bids and by evaluating all proposals, both public and private, under the same set of rules (the FAR) and allowing agencies to make decisions based on cost or on cost technical trade-offs. For the first time, public sector employees will be allowed to make offers based on best value, thereby encouraging innovation from those who are most familiar with the work – the Government workforce.

Under the old A-76 process, the public sector proposal was driven primarily to slash cost, reduce personnel, and only meet the minimum performance level required by the statement of work. Under a FAR-based process, public sector employees would be encouraged to come up with innovative approaches and solutions, not discouraged by a process in which cost is the only factor.

Creating the situation (as the old A-76 rules did) where Government organizations are ultimately competing with the private sector on a cost rather than a quality-dominated basis is in sharp contrast with the quality/best value principals that were strongly enunciated in the National Performance Review. Ironically, as Government acquisition policy has significantly moved away from price as a key factor and toward best value, the old A-76 process for public-private competitions continued to require simplistic cost comparisons.

The importance of "best value" procurements has been highlighted in the House Armed Services Committee Report on the 1994 Federal Acquisition Streamlining Act. The report states, "*The committee notes that, over the past decade, the acquisition system has become more complex and sophisticated. This has made it increasingly important to balance quality discriminators, such as technical capabilities, against price and other considerations in the source selection process. Therefore, the committee believes that the use of value-based contracting or 'best value' is long overdue and that this will cause contractors to perform better and to produce better products."*

Some have argued that "best value" is, by its very nature, subjective. I would not agree. Best value may not mean the same thing in every instance, but there is no reason why the Government should not be able to define, with reasonable precision, what best value means on a specific solicitation. Best value should give the Government the flexibility to buy precisely what it needs, with a responsible balance between price and

features. And, consideration of best value should always include past performance because best value is unlikely to be provided by a contractor with a poor record of prior performance. Nor should best value be used to protect popular incumbents or to eliminate competent but lower priced offers from an A-76 competition. In order to achieve these goals, award criteria should be clearly and unambiguously set forth in the solicitation, and should be specifically tailored to the requirements of the mission, system or installation.

As I have already mentioned, the Revisions allow for best value, but as the Federal Register rightly noted, *"the Circular will continue to require the meaningful consideration of cost as a factor in all public-private competitions."* Best value does indeed equal quality and cost!

Accountability

The Revisions enhance the accountability associated with competitive sourcing. The FAR-type approach offers a procurement process that is more transparent than the old A-76 process. Conflict of interest rules are more clearly defined. Competition officials and individuals participating in the process must comply with procurement integrity, ethics and standards of conduct rules.

Most important, if the public sector wins the competition, its proposal will be treated like a contract ("letter of obligation"). This means that Government officials will monitor the cost and service performance levels of the public sector's Most Efficient Organization (MEO). The MEO's performance will now become a past performance factor – the basis for whether they can win future work, just like a contractor.

One criticism has been that there is no system in place to hold contractors accountable, or mechanisms for tracking the cost and quality of service contracting. Unfortunately, the myth that contractors are not accountable continues to be perpetuated, despite rigorous accountability during competition, during performance of the work, and at the end of the contract.

Virtually all service contract work is subject to intense competition between private sector competitors. These competitions are closely monitored by Federal officials and subject to pricing, conflict of interest and past performance evaluation under strict guidelines.

The FAR requires private sector contractors to open their books and records for financial audits. Types of audits performed under a typical Government contract include: pre-award audits; periodic financial audits during the contract; invoice audits; incurred cost audits; and final closeout audits just to name a few. The FAR also requires most service contracts to contain a myriad of other requirements, governing labor and compensation, safety and environmental regulations – all subject to oversight and audits. With regard to performance, most of our service contracts require quarterly reviews. Our

customer examines every aspect of our work to determine if we are meeting the performance metrics detailed under our contract.

Under the Revisions, now all providers – including the public sector – will be scrutinized to ensure that they (public or private) make *"good on their promises to the Government."* (Federal Register notice, May 29, 2003). And agencies will be required to track the execution of both streamlined and standard competitions, again no matter who the provider is (public or private sector).

Disagreements with the Final Circular A76 Revisions

Overall, we are very optimistic over the intent and ultimate implementation of the final A-76 Revisions. However, there are a few areas on which I would like to share our concerns:

Transmittal Memorandum

> *"The longstanding policy of the federal government has been to rely on the private sector for needed commercial services. The competitive enterprise system, characterized by individual freedom and initiative, is the primary source of national economic growth."*

This has been a fundamental premise since 1954, and supported by both Democratic and Republican Administrations.

I would like to register the concern of CSA members over the elimination of not only this longstanding Government policy statement related to reliance on the private sector, but also the elimination of the presumption in the proposed November 2002 that "all activities are commercial in nature." We recognize that the current Administration's general policy, as noted in the Federal Register notice, is a reliance on competition. However, we do not believe that the policy statements in question are contrary to that policy. We would urge that the policy statement in effect since 1954 be included in the Circular.

Direct Conversion

CSA members have long supported the ability of agencies to directly convert work to the private sector. This increases agency flexibility to ensure it is receiving the best value to meet its mission needs. It would also help agencies in meeting their small business goals. Therefore, we are concerned over the total elimination of the direct conversion process.

For now, we will reserve comment on the streamlined process. We recognize the intent, and we sincerely hope that agencies will indeed avail themselves of the process, rather than deciding it is too hard to accomplish in the timeframe allowed, and either not do anything or use the standard competition. The "devil will be in the details" to ensure

its proper implementation. We would suggest that consideration be given to increasing the threshold from 65 to 100 FTES. And, we do applaud the elimination of the differential in the streamlined process since this will ensure that agencies have the necessary latitude to make decisions based on their market research. At some point, we would suggest that OMB review the feasibility of eliminating this differential for standard competitions as well.

One concern, for either side, is that there is no appeal process – even at a contracting officer level – to challenge an agency decision. Such an appeal process would necessarily be structured to be very limited (e.g., tight timeframes), but it may be necessary to ensure fairness.

[Note: While the Revisions do not specifically state this, current statutes (e.g., the annual Defense appropriations acts) allow for direct conversion to Native American-owned businesses; we presume that nothing in the revised Circular is counter to those statutory requirements.]

Inter-Service Support Agreements (ISSAs)

The proposed November 2002 Revisions included important modifications related to Inter-Service Support Agreements (ISSAs). Unfortunately, this section was eliminated from the final Revisions issued on May 29, 2003.

The Revisions noted that Circular No. A-97 remains in effect. However, modifications to the Circular addressing recompetition and "grandfathering" of certain ISSAs, which had been proposed in 2001, have never been formally adopted. The November 2002 proposal would have put into effect those modifications by ensuring that all ISSAs are subject to recurring recompetition as well – including both new agreements as well as those originally grandfathered out of any competition requirement. This was a step in the right direction toward ensuring that Federal agencies obtain the best value for the American taxpayer. The 2001 proposed changes to A-97 are not addressed in the Revisions issued on May 29 and, therefore, are still in question.

CSA, along with its industry counterparts, has long been concerned that interservicing agreements among Federal agencies, as well as the military services, are used as a means to avoid outsourcing and privatization. We do not believe that ISSAs should be exempt from competition. Requiring the use of competitive procedures for all ISSAs is consistent with the Economy Act (31 U.S.C. 1535), the Intergovernmental Cooperation Act (31 U.S.C. 6505), and the intent of the Federal Activities Inventory Reform (FAIR) Act (P.L. 105-270) and the Government Management and Reform Act of 1994 (103 U.S.C. 356).

Other Issues related to the A-76 Process

I would like to highlight a few other issues related to the A-76 Process that were not specifically addressed in the Revisions.

Protest Rights

Since the public sector is competing under the same set of rules and is treated as a true bidder, the MEO should have the right to protest to the General Accounting Office (GAO) or file in the United States Court of Federal Claims to resolve competition disputes. The proposed Revisions are silent on this particular issue, presumably leaving the question to be resolved by GAO and the Court. However, logical reasoning and fairness led the Commercial Activities Panel to recommend that appeal rights be given to the public sector. In other words, if the public-sector team (represented by the Agency Tender Official) is truly treated as a bidder, it should have protest rights.

On June 13, 2003, the GAO issued a notice soliciting comments regarding two key legal questions related to protest rights for the agency MEO. CSA, along with other industry associations, will be providing comments on the issues raised by GAO.

Treatment of Workers

Taking care of Government workers who are impacted by outsourcing decisions is an issue the private sector takes very seriously. Former Government workers affected by a conversion of their jobs to contract are typically offered a "right of first refusal," under which the workers are given first priority for employment for those jobs for which they are qualified – and this is recognized in the Revisions. In many instances, persons stymied in their desire for promotion find that working for a contractor provides upward mobility they did not previously enjoy. Contractors are not typically strictly bound by seniority in making employment decisions. As a result, dramatic improvements in a workforce can be achieved just by selecting highly qualified personnel for supervisory and/or key technical positions. This infusion of fresh enthusiasm can invigorate a workforce even when the workforce as a whole remains relatively unchanged due to "right of first refusal" protections. Furthermore, responsible contractors understand that satisfied customers depend, to a considerable degree, upon satisfied employees. All responsible contractors treat benefits management as an important element of good labor relations.

It has been said that contractors have incentives to reduce costs by requiring inferior compensation packages for those who perform Government work. The fact is that the Service Contract Act (or the Davis-Bacon Act) governs the vast majority of wages paid by Federal service contractors to their employees. If there is concern over the compensation packages for service contract employees, it should be directed to the current wage and benefits standards set by Department of Labor, not the competitive sourcing process.

Finally, there should be early engagement with Federal employees to both keep them informed and answer their questions regarding the uncertainty of the process.

Performance Based Services Acquisition

The November 2002 proposed Revisions stated that a Performance Work Statement (PWS) "that is developed in a Standard Competition shall be performance-based with measurable performance thresholds and may encourage innovation." While this specific statement is not included in the final Revisions, we presume that contracting officers will continue to be encouraged to use performance-based contracts. This process specifies the Government's objectives in terms of outcomes or results, but leaves it to the contractor to determine the best way to achieve them.

However, training remains the number one stumbling block to full and successful implementation of performance-based contracting. It must be enhanced if performance based services acquisition (PBSA) is to become successfully implemented. PBSA requires new evaluation techniques, new management approaches (involving the entire acquisition team) and improved contract relationships.

Small Business Considerations

We remain hopeful that the one voice that has not been widely heard in the debate over A-76 – small business – would receive a fairer hearing under the FAR-based process. Few, if any, small businesses today can afford to compete on an A-76 competition. The 2-4 year time lag alone (in the current A-76 process) made the old process prohibitively expensive for small businesses. Will a FAR-based process ensure fairness for small businesses? We believe it will.

But there are certain issues that must be considered that were not specifically addressed. These deal with small business set-asides, minority business preference programs (e.g., 8a or small disadvantaged businesses set-asides), and HUBZones, as well as Native American preferences, and disabled-veteran and women-owned small business preferences. CSA membership includes many small companies that fall within these categories – and we want to ensure that the FAR programs and protections currently in place will be continued.

Conclusion

The challenge we face today is to implement this new public-private competition process – one that encourages competition, treats public sector employees with respect, and provides for a fair system under which all competitors, public and private, are judged under the same set of rules. The spirit of the Revisions lives up to that challenge.

Thank you for this opportunity to testify.